



**UNITED STATES ENVIRONMENTAL PROTECTION AGENCY  
REGION 8**

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08/21/2023

Ms. Tina McFarling, P.E.  
Program Administrator  
Environmental Funding Program  
Joe Foss Building, 523 E. Capitol  
Pierre, SD 57501

Dear Ms. McFarling:

The U.S. Environmental Protection Agency (EPA) Region 8 has conducted an annual review of the South Dakota Clean Water State Revolving Fund (CWSRF) for federal fiscal year 2022 (FY22) (October 1, 2021 through September 30, 2022), which matches the South Dakota state fiscal year, in accordance with EPA's SRF Annual Review Guidance.

The South Dakota Department of Agriculture and Natural Resources (DANR) manages the engineering and financial aspects of its CWSRF. As of September 30, 2022, the CWSRF operates as a direct loan program that episodically uses a cash-flow leveraging structure to sell additional bonds if warranted by project demand. Interest rates for FY22 loans typically ranged from 1.875 percent to 2.125 percent, which included a 0.25 percent surcharge that is used for a wide range of activities, including nonfederal cost-share for total maximum daily load (TMDL) assessment and implementation projects, planning grants, and to supplement the consolidated program with grants for wastewater treatment projects.

The scope of the annual review covers October 1, 2021 to September 30, 2022 and includes consideration of the legal, managerial, technical, financial, and operational capabilities of the state related to the CWSRF. EPA visited the state offices in Pierre, South Dakota during the week of June 5th, 2023. Activities incorporated into the annual review included an analysis of the FY22 and FY23 Intended Use Plans (IUPs), FY22 audited financial statements, two project files (Mitchell and Hartford), South Dakota financial indicators, and the following four cash draws:

CS460001-20; \$288,000; October 13, 2021  
CS460001-20; \$170,400; January 13, 2022  
CS460001-21; \$86,500; June 28, 2022  
CS460001-21; \$136,900; September 22, 2022

**Observations**

The state of South Dakota manages its base CWSRF program in accordance with applicable statutes, regulations, and guidance. The EPA, Region 8, lists program observations below. Attached to this report is a table that shows each indicator in further detail. The South Dakota CWSRF cash draws tested for this annual review all complied with 40 CFR Part 35.3155(d)(5), which requires that cash draws will occur at a 83.33 percent federal proportionate share (and match will be at 16.67 percent), or that 100

percent of the match will be disbursed prior to the state drawing federal cash from a specific grant. The state is spending the entire match amount for the grant prior to drawing federal funds. However, as of November 18, 2022, recipients are no longer required to comply with the cash draw rules. If a grant that was awarded prior to November 18, 2022, is amended to include this term and condition, the recipient is no longer required to comply with the above-cited regulations.

In November 2021, the Bipartisan Infrastructure Law (BIL) was signed into law, which appropriated additional federal CWSRF funding for FY22-FY26 through two types of clean water grants: BIL general supplemental and BIL emerging contaminants. In March 2022, EPA issued BIL Implementation Guidance with the following FY22 allotments for South Dakota:

Supplemental: \$8,738,000  
Emerging Contaminants: \$459,000

The FY23 allotments for South Dakota were issued on April 3, 2023, as follows:

Supplemental: \$10,233,000  
Emerging Contaminants: \$1,043,000

Throughout the five years of BIL Implementation, EPA expects South Dakota to:

- Evaluate and revise, as needed, its CWSRF affordability criteria;
- Evaluate the CWSRF's priority point system for project ranking commensurate with need;
- Consider technical assistance funding; and
- Engage residents and community stakeholders in disadvantaged communities.

### **Unliquidated Obligations**

At the end of FY22, The South Dakota CWSRF had approximately \$7 million in unliquidated obligations (ULOs), which equals a 97 percent federal outlay expenditure rate, a slight improvement from last year. The state typically spends a CWSRF grant in approximately two years from time of award. For the overall "flow of South Dakota CWSRF funds", as of September 30, 2022, the percentage of total construction disbursements (\$812.9 million) divided by total CWSRF funds available (\$1,111.2 million) is 73 percent, which is a one percent decrease from last year., This is an excellent result given the large influx of BIL funds.

### **CWSRF Project Progress**

The CWSRF is summarized as of September 30, 2022, in Table I, which presents loan fund information and pace of construction.

TABLE I: CWSRF Program Summary (\$ millions)				
CWSRF Funds Available	Project Assistance	Fund Use Rate	Project Disbursements	Pace of Construction
\$1,111.2	\$1,061.1	95%	\$812.9	77%

As of September 30, 2022, South Dakota's CWSRF *Fund Use Rate* was at 95 percent, with the uncommitted five percent equaling \$50.1 million. This was an increase of the FY21 fund use rate of four percent. South Dakota FY23 IUP identified \$176.9 million in projects to be funded in FY23. The FY23 fundable list includes a \$38.5 million dollar project in Mitchell, a \$35.5 million dollar project in Sioux Falls, and a \$10.3 million dollar project in Sturgis. Therefore, the program has sufficient planned projects to spend the uncommitted funds.

The improved fund use rate is also an indication that the influx of American Rescue Plan Act (ARPA) funds is starting to have less impact on the SRF program. Last year, the SRF program faced direct competition from the ARPA program that committed approximately \$600 million of ARPA grant funds to drinking water and wastewater projects, making SRF loans less appealing to communities.

In FY22, the CWSRF spent \$63.1 million in construction expenses, and the *Pace of Construction* (disbursements divided by total project amounts) decreased from 81 percent to 77 percent. Relative to the \$63.1 million in construction expenses spent in FY22, the state spent \$2.1 million in federal cash draws in FY22 and South Dakota's *Federal Return* increased from 3.48 to 3.73, a good result. Overall, South Dakota SRF staff manages projects very well.

A key component of strategic SRF fund management is the balancing of cash inflows and outflows. The following ratio shows how efficiently South Dakota's CWSRF is revolving by examining the program's disbursement rate over a set time-period and comparing it to the amount of cash on hand. The ratio is calculated by subtracting total project disbursements (\$812.9 million) from total funds available (\$1,111.2 million) and comparing this number (\$298.3 million) to the average annual disbursements over the past three years (\$42.5 million). For the South Dakota CWSRF, this ratio is 7.02 (years), which is an increase from last year's ratio of 5.30. This is an expected result since the state sold \$100 million in bonds in FY21 drastically increasing the funds available amount. However, this was in anticipation of an increase in funding demands as seen in the state's current IUP project lists.

South Dakota CWSRF project milestones accomplishments as of June 30, 2022 are as follows (in \$ millions):

- Project Assistance: 496 projects at \$1,033.9
- Construction Starts: 464 projects at \$1,012.1
- Project Completions: 415 projects at \$666.1

Overall, the South Dakota CWSRF is performing well in working with local governments to build treatment works and other water quality projects to further the goals of the Clean Water Act. South Dakota's ratio of project completions to total project assistance is 64%, which is 4 percent lower than the national CWSRF average of 68 percent. This value is not unexpected given the large projects currently under construction.

### **Green Project Reserve, Additional Subsidy, and Equivalency**

South Dakota has met its Green Project Reserve requirements through its FY21 grant. Additionally, the Sioux Falls Water Reclamation Facility expansion will replace a significant amount of mechanical equipment. This project will provide sufficient funds to meet the 10 percent requirement of the FY22 capitalization grants. Once equipment replacement total is determined, the GPR amount will be updated in the SRF data system.

Regarding additional subsidy, the state has provided \$3.1 million in principal forgiveness, which is the maximum amount allowed for the FY21 grant. For the FY22 grants, including BIL general supplemental grant, the FY23 IUP shows over \$10 million dollars of principal forgiveness to be funded in FY23.

For equivalency, to date South Dakota has funded equivalency projects through the FY21 grant requirement. They are continuing to work on the FY22 grant requirement.

### **Financial Sustainability**

Based on information from Clean Water National Information Management System (Clean Water NIMS), the CWSRF had a cumulative *Net Return (not including Subsidy)* amount of \$35.9 million as of June 30, 2022, an annual decrease of \$5.5 million. In FY22, the state collected \$5.9 million in interest payments and collected an additional \$3.8 million in interest earnings on investments and paid \$13.3 million in bond interest expense and repaid \$1.8 million in state match bonds.

The *Net Return on Contributed Capital excluding Subsidy* (contributed capital being the sum of federal outlays for loan fund and deposited state match) was 13.8 percent. These dollar amounts and percentages show that the state has managed CWSRF fund accounts well and is maintaining the contributed capital for its CWSRF without making adjustments for loss of purchasing power due to inflation.

### **Total Net and Net Interest Margin**

*Total Net* measures the extent by which internal growth is generating additional funding for new projects. This is calculated by taking the total cash inflows generated by ongoing loan and investment activity less bond repayments and interest payments. New federal capitalization grants are excluded from this calculation. As of June 30, 2022, the South Dakota CWSRF's *Total Net* was a strong \$20.4 million.

*Net Interest Margin* measures the percentage rate of return the SRF is generating from its total assets through loans and investments less bond interest expense. For FY22, the South Dakota CWSRF's *Net Interest Margin* was 0.8%, based on an annual net interest amount of -\$3.6 million and an average of total assets of \$586.2 million and \$601.7 million at the beginning and end of FY22, respectively (average total assets calculated using the FY22 and FY21 total assets from the SD audited financial statements).

### **Financial Management and Proportionality**

The South Dakota CWSRF has had no defaults and municipal loans are typically secured by revenues from user charges. The total net position (based on audited financial statements) plus undrawn federal grant funds as of June 30, 2022 was \$275.4 million, little over two percent increase over the FY21 net position of \$270.5 million. Since the state has deposited and disbursed state match prior to drawing federal funds, all four cash draws listed on page one above were done with a 100 percent federal proportion. Furthermore, the payment requests for the cash draws were for eligible costs and were adequately documented. No costs were questioned and there were no improper payments.

For the year ending June 30, 2022, the South Dakota Department of Legislative Audit issued an SRF financial statement and compliance audit report on October 21, 2022. There were no findings/recommendations from either audit.

### **Prior Recommendations**

There were no recommendations from last year's review.

**New Recommendations**

There are no new recommendations with this review.

The South Dakota CWSRF assessment has been completed by SRF Coordinator, Lindsey Phillips, in collaboration with the EPA Region 8 SRF team. If you have questions, you may contact Lindsey at Phillips.Lindsey.A@epa.gov or (303) 312-7291.

Sincerely,

Benjamin Bents  
Branch Manager  
Technical and Financial Services Branch

cc: Mr. Andy Bruels, P.E., Division Director